

Message Text

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ACTION EUR-08

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FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC IMMEDIATE 6863

C O N F I D E N T I A L SECTION 01 OF 02 OTTAWA 01595

LIMDIS

DEPARTMENT FOR EUR/CAN AND EB; DEPARTMENT PASS DOE FOR LES
GOLDMAN, ASST. SECRETARY BERGOLD; DOE/FERC FOR COMMISSION-
ER SMITH AND JOHN ADGER

E.O. 11652: GDS
TAGS: ENRG, PGOV, SENV, CA
SUBJECT: ALASKA HIGHWAY GAS PIPELINE: FERC PROPOSED
PRESS RELEASE AND Q&A TALKING POINTS ON CHOICE OF PIPELINE
SIZE

1. EMBASSY HAS REVIEWED PROPOSED PRESS RELEASE AND INFOR-
MATION PACKAGE PREPARED BY FERC AND SUGGESTS FOLLOWING
CHANGES:

2. WE FEEL THAT PRESS RELEASE SHOULD INCLUDE DATA ON 48-
INCH LOW-PRESSURE BASE CASE AND 48-INCH HIGH-PRESSURE
SYSTEMS IN ADDITION TO 54-INCH AND 56-INCH DATA PROVIDED.
IF THIS ADDITIONAL DATA IS ADDED TO RELEASE, IT SHOULD
ALSO INCLUDE BRIEF STATEMENT OF NATIONAL ENERGY BOARD
(NEB) RATIONALE FOR SELECTION OF A LARGE-DIAMETER, LOW-
PRESSURE SYSTEM RATHER THAN 48-INCH HIGH-PRESSURE SYSTEM.
STATEMENT SHOULD STRESS FOLLOWING NEB CONCERNS: (1) SAFE-
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TY AND RELIABILITY, (2) POTENTIAL DELAY WHICH WOULD RESULT
FROM REQUIREMENT TO BURST TEST 48-INCH HIGH-PRESSURE
SYSTEM BEFORE DECIDING ON SELECTION OF THAT TECHNOLOGY,
AND (3) LIKELY DIFFICULTY OF PRODUCING SUFFICIENT QUANTI-
TIES OF 48-INCH, HIGH-PRESSURE PIPE IN TIME TO MEET CON-
STRUCTION SCHEDULE.

COMMENT: WE SUGGEST THIS CHANGE BECAUSE CRITICAL, CONTENTIOUS ISSUE HAS BEEN CHOICE BETWEEN 48-INCH, HIGH-PRESSURE U.S. LARGER DIAMETER, LOW-PRESSURE SYSTEM, NOT 54-INCH U.S. 56-INCH SYSTEM. WE SUGGEST ADDING BASE CASE DATA TO BALANCE PRESENTATION.

3. FOLLOWING ARE SUGGESTED REVISIONS OF FOUR OF THE EIGHT QUESTIONS AND ANSWERS.

-----A. QUESTION: SECTION 7 OF THE AGREEMENT BETWEEN THE U.S. AND CANADA CALLS FOR COMPETITIVE BIDDING. THE LEGISLATION BEING CONSIDERED BY THE CANADIAN PARLIAMENT TO AUTHORIZE THE JOINT PROJECT CONTAINS A CONDITION REGARDING MAXIMIZING CANADIAN CONTENT. DOESN'T THIS VIOLATE THE TERMS OF THE AGREEMENT?

ANSWER: NO. SECTION 7 STATES THAT EACH GOVERNMENT WILL ENDEAVOR TO INSURE THAT GOODS AND SERVICES TO THE PIPELINE PROJECT WILL BE ON GENERALLY COMPETITIVE TERMS. CANADIAN FIRMS SHOULD ENJOY LOCATION ADVANTAGES THAT WOULD TEND TO MAKE THEM MORE COMPETITIVE, HENCE, WE NORMALLY WOULD EXPECT A HIGH CANADIAN CONTENT IN ANY EVENT CANADIAN LEGISLATION MOREOVER DOESN'T VIOLATE THE TERMS OF AGREEMENT. SCHEDULE III (TERMS AND CONDITIONS OF THE BILL) SPECIFIES THAT THE CANADIAN PIPELINE COMPANY SHALL DESIGN A PROGRAM FOR THE PROCUREMENT OF ALL GOODS AND CONFIDENTIAL

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SERVICES FOR THE PIPELINE THAT ENSURES THAT CANADIANS HAVE A FAIR AND COMPETITIVE OPPORTUNITY TO PARTICIPATE IN THE SUPPLY OF GOODS AND SERVICES FOR THE PIPELINE. THE REQUIREMENT THAT CANADIAN CONTENT BE MAXIMIZED IS IN THE CONTEXT OF THE REQUIREMENT THAT CANADIAN FIRMS HAVE "AN OPPORTUNITY TO COMPETE" AND OF THE REQUIREMENT IN OUR BILATERAL AGREEMENT FOR "GENERALLY COMPETITIVE TERMS." IF IT APPEARS THAT THE OBJECTIVES OF PARAGRAPH 7 ARE NOT BEING MET, THE U.S. MAY INSTITUTE CONSULTATIONS WITH THE CANADIANS. ALSO, THE FERC MUST APPROVE ALL CAPITAL COSTS TO BE INCLUDED IN A RATE BASE. THUS, THE U.S. SHOULD BE ABLE TO HAVE REMEDIES SHOULD IT APPEAR THAT CANADIAN COSTS WERE NOT GENERALLY COMPETITIVE.

COMMENT: WE FEEL THIS REVISION RESPONDS MORE DIRECTLY TO QUESTION WHETHER CANADIAN LEGISLATION VIOLATES AGREEMENT.

-----B. QUESTION: WILL NOT THE CANADIAN CONTENT CONDITION ATTACHED TO THE CANADIAN LEGISLATION EXCLUDE U.S. FIRMS FROM SECURING CONTRACTS FOR SERVICES OR EQUIPMENT?

ANSWER: ANY RESTRICTIONS ON CANADIAN CONTENT SET BY THE

NATIONAL ENERGY BOARD WILL BE MORE IN THE NATURE OF GUIDELINES THAN OF ACTUAL RESTRICTIONS. IN ADDITION, THE SEVERITY OF SUCH RESTRICTIONS DEPENDS TO A GREAT EXTENT UPON THE DEFINITION OF CANADIAN CONTENT. EQUIPMENT SUPPLIED BY A U.S. FIRM WITH MANUFACTURING OR ASSEMBLY FACILITIES IN CANADA WOULD QUALIFY AS 100 PERCENT CANADIAN CONTENT EVEN THOUGH A PORTION OF EQUIPMENT MAY HAVE BEEN MANUFACTURED IN THE U.S. AND A LARGE PORTION OF ANY PROFITS MAY RETURN TO THE U.S. IN ADDITION, U.S. CONSTRUCTION COMPANIES WITH CANADIAN PARTNERS, AND HIRING PREDOMINANTLY CANADIAN LABOR, WOULD QUALIFY UNDER THE CANADIAN CONTENT PROVISION. FURTHER, CANADIAN CONSTRUCTION FIRMS HAVE TRADITIONALLY PURCHASED AND WILL LIKELY CON-

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C O N F I D E N T I A L SECTION 02 OF 02 OTTAWA 01595

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TINUE TO PURCHASE, LARGE AMOUNTS OF U.S. EQUIPMENT. THUS, EVEN CONTRACTS TO 100 PERCENT CANADIAN FIRMS MAY GENERATE MANY U.S. ORDERS FOR EQUIPMENT.

THE PRIMARY AREA WHERE A CANADIAN CONTENT PROVISION MIGHT IMPACT U.S. FIRMS WOULD BE IN THE SUPPLY OF STEEL PIPE. U.S. FIRMS CANNOT MAKE 56-INCH PIPE WHICH WILL BE USED IN APPROXIMATELY 55 PERCENT OF THE LINE IN CANADA. HOWEVER, THEY MAY BID ON THE PIPE FOR THOSE SECTIONS OF THE LINE IN CANADA DESIGNED FOR 48-INCH, 42-INCH, OR 36-INCH PIPE.

COMMENT: WE HAVE DELETED LAST TWO SENTENCES DEALING WITH ISSUE OF POSSIBLE COMPETITION FROM OUTSIDE NORTH AMERICA BECAUSE GOC WILL NOT ALLOW IT TO ARISE. IF WE DEAL WITH

THIS ISSUE AT ALL IT SHOULD BE TREATED IN SEPARATE Q&A.

-----C. QUESTION: THE AGREEMENT BETWEEN THE U.S. AND CANADA CALLS FOR THE U.S. TO PAY FROM TWO-THIRDS TO ALL OF THE COST TO BUILD A CONNECTING PIPELINE BETWEEN DAWSON, YUKON AND WHITEHORSE, YUKON TO DELIVER CANADIAN GAS TO WHITEHORSE. WHY SHOULD THE U.S. CONSUMERS BE FORCED TO CONFIDENTIAL

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PAY FOR THIS PIPELINE?

ANSWER: THE CANADIAN NATIONAL ENERGY BOARD APPROVED A PIPELINE ROUTE THROUGH CANADA THAT WENT THROUGH DAWSON, YUKON RATHER THAN THE PRESENT ROUTE SOUTH OF DAWSON. THIS ROUTE WAS NOT ACCEPTABLE TO OUR GOVERNMENT SINCE IT BOTH INCREASED THE LENGTH OF THE PIPELINE AND INCREASED THE LENGTH OF THE LINE IN THE DISCONTINUOUS PERMAFROST REGION, WHERE PIPELINE COSTS WILL BE HIGHEST. UNITED STATES ANALYSTS DETERMINED IT WOULD BE CHEAPER FOR U.S. CONSUMERS TO BUILD THE LINE AS PLANNED AND PAY FOR THE ADDITIONAL CANADIAN LINE FROM DAWSON TO WHITEHORSE, THAN IT WOULD BE TO CONSTRUCT A DIVERTED LINE THROUGH DAWSON. FURTHER, THE AGREEMENT PROVIDES THAT THE LEVEL OF U.S. FUNDING OF CAPITAL COSTS ON THE DAWSON-WHITEHORSE SEGMENT WILL BE DETERMINED BY CANADIAN SUCCESS IN MINIMIZING COST OVERRUNS. THE POTENTIAL REDUCTION IN COST-OF-SERVICE TO CANADIAN CONSUMERS OF MACKENZIE DELTA GAS WILL BE A SIGNIFICANT INCENTIVE FOR THE CANADIAN GOVERNMENT AND PIPELINE COMPANIES TO REDUCE CONSTRUCTION COSTS ON THE MAIN TRUNK SYSTEM AND THUS BENEFIT AMERICAN CONSUMERS AS WELL. CONSEQUENTLY, THE U.S. GOVERNMENT PROPOSED THE PRESENT PLAN IN LIEU OF THE ROUTE APPROVED BY CANADA. AFTER CONSIDERABLE NEGOTIATIONS THE U.S. PROPOSAL WAS ACCEPTED BY THE CANADIANS. THE PRESENT PLAN WAS ADOPTED RATHER THAN THE ROUTE ORIGINALLY APPROVED BY THE CANADIANS, SINCE IT WILL YIELD A LOWER COST OF SERVICE TO U.S. CONSUMERS.

COMMENT: WE DELETED SENTENCE SAYING CANADA MIGHT NOT BUILD DEMPSTER LATERAL BECAUSE IT CONFLICTS WITH STATED GOC POLICY AND ASSURANCES THEY HAVE GIVEN US. SUBSTITUTED LANGUAGE REFLECTS MUTUAL ADVANTAGES OF THIS PORTION OF AGREEMENT.

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-----D. QUESTION: THE U.S. ORIGINALLY ESTIMATED THAT THE

INCREASED COST OF A 56-INCH PIPELINE WOULD BE ONLY \$12
MILLION MORE THAN FOR A 54-INCH PIPELINE. WHY DO WE NOW
AGREE THAT THE COST WOULD BE \$91 MILLION MORE?

COMMENT: WE HAVE NOT REVISED ANSWER TO THIS QUESTION.
WE RECOMMEND, HOWEVER, THAT FERC STAFF WHO ARE MORE
FAMILIAR THAN WE WITH CAPITAL COST CALCULATIONS ADD PAS-
SAGE TO DEAL WITH USG-GOC DIFFERENCES OVER \$36 MILLION
DISCREPANCY AND USG VIEW THAT THIS AMOUNT WOULD BE ATTRIB-
UTABLE TO MONITORING COSTS. QUESTIONS ON DISCREPANCY
ARE BOUND TO COME UP. ALSO, LAST PARAGRAPH OF ANSWER RE-
FERS TO "INCREASED COST OF \$179 MILLION (1984 DOLLARS)
COMPARED TO THE U.S. ESTIMATE OF \$58 MILLION." SHOULDN'T
THIS READ 1974 DOLLARS RATHER THAN 1984 DOLLARS?
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